

**Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554**

In the Matter of)	
)	
Petition for Rulemaking or, Alternatively, a)	RM-11019
Waiver of the Closed Bidding Rules for C)	
Block Licenses in the Broadband Personal)	
Communications Services)	

Comments of The Progress & Freedom Foundation

The Progress & Freedom Foundation (PFF) is a private, non-profit, non-partisan research institution established in 1993 to study the digital revolution and its implications for public policy. PFF hereby submits these reply comments in support of CTIA’s “Petition for Rulemaking or, Alternatively, a Waiver of the Closed Bidding Rules for C Block Licenses.”¹ PFF supports a free, open market for spectrum licenses as best for consumers, and opposes the Designated Entity (DE) set-aside as contrary to a market system. By removing the DE restriction on certain Auction No. 58 licenses and in future auctions, the Commission will make for a more competitive auction process, where spectrum will more cheaply and quickly find its way to providers who value it most. In the end, this will benefit consumers because providers will have lower costs and spectrum will be used more efficiently.

The Nature of Today’s Wireless Market Necessitates an Open Bidding Process

Commenters present several legal and policy rationales against the removal of closed bidding in Auction No. 58 and future C Block auctions. The Designated Entity Program Supporters (DEPS) argue, among other things, that set-asides are “essential” in furthering the Congressional goals housed in section 309(j) and the legislative history

¹ The views expressed in these comments are those of the author and do not necessarily reflect the views of the directors, officers or staff of the Foundation.

behind the Omnibus Reconciliation Act of 1993 provides the basis for this result.² Of course, the Commission has emphasized that it has “wide latitude in determining how to achieve” the objectives under section 309(j), which “does not mandate the use of set asides.”³ Additionally, the same House Budget Committee Report offered by DEPS to explain Congressional concern for small businesses also advised that these considerations must be balanced against the nature of the service offered.⁴ As one article explains:

The committee’s concern in disseminating licenses among small businesses was to prevent a significant increase in the concentration of the telecommunications industries, while recognizing that “the characteristics of some services are inherently national in scope, and therefore ill-suited for small business.” The committee observed that those services with *local* characteristics could “provide new opportunities for small business participation.” *In those cases*, the committee anticipated that the FCC would ensure that small businesses would not be excluded due to the competitive bidding system. (emphasis in original, citations omitted).⁵

T-Mobile notes that the Commission’s C and F block bidding rules were “created at a time when the future evolution of the marketplace was undefined and governed by a cellular duopoly.”⁶ Today, six national carriers and a number of regional operators exist in a highly competitive market. Recent Commission data illustrate that the wireless market is mature, with 95 percent of the nation’s population living in counties with access to three or more providers.⁷ The Commission has concluded that wireless carriers are “competing effectively” in rural service areas, which have an average of 3.3 competitors.⁸ In this market, scale matters. According to economist and auction expert Peter Cramton:

² Opposition of Designated Entity Program Supporters at 3.

³ *In the Matter of Amendment of the Commission’s Rules Regarding Installment Payment Financing for Personal Communications Services (PCS) Licensees*, Sixth Report and Order and Order on Reconsideration, WT Docket No. 97-82, at ¶ 22 (Rel. Aug. 29, 2000).

⁴ H.R. Rep. No. 103-111, at 253 (1993).

⁵ Mark W. Munson, *A Legacy of Lost Opportunity: Designated Entities and the Federal Communication Commission’s Broadband PCS Spectrum Auction*, 7 MICH. TELECOMM. TECH. L. REV. 217, 224 (2001).

⁶ Comments of T-Mobile USA, Inc., Executive Summary.

⁷ *In the Matter of Implementation of Section 6002(b) of the Omnibus Reconciliation Act of 1993*, Eighth Report, WT Docket No. 02-379, at ¶ 18 (Jul. 14, 2003). 97 percent of the population lives in counties where at least one provider offers digital service. *Id.* at ¶ 78.

⁸ *Id.* at ¶¶ 113, 120.

[W]hat we have learned in the last several years is that there are significant scale economies in wireless communications. Part of the scale economy is the bargaining advantage it creates with equipment suppliers. Another part is scale economies in marketing. But perhaps the largest is the value that consumers place on seamless nationwide roaming. As a result, the marketplace has shifted toward nationwide services in most wireless categories. These nationwide services are necessarily billion dollar deals, or tens-of-billions in the case of broadband mobile services. What consumers need is a variety of strong national competitors. In many cases, the small regional players cannot compete. The designated entity rules may simply be setting up the small business for failure.⁹

By eliminating the DE set-aside, the Commission can allow the scale economies to be achieved, while still maintaining a competitive market. As it stands now, the DE rules artificially parse the market for the benefit of regulation-created entities that would not otherwise exist but for FCC set-asides. Against this, the Commission needs to weigh the consumer benefits from an open, free market in spectrum. On this scale, the balance surely tips toward consumers.

Closed Bidding Harms Consumer Welfare and Creates a Perverse Set of Incentives for Designated Entities

Commenters also make the general claim that “[t]he overwhelming success of Auction No. 35 demonstrated that DEs will participate in the auction process when they have meaningful incentives (in the form of set-asides combined with bidding credits).”¹⁰ This argument is unavailing. Close scrutiny of the results of Auction No. 35 compels a different analysis: namely, that national or regional carriers, or DEs “backed” by these carriers through exceptions in the Commission’s eligibility rules,¹¹ were the high bidders for a substantial majority of licenses available through both open and closed bidding.¹²

⁹ Peter Cramton, *Lessons from the United States Spectrum Auctions*, prepared testimony before the United States Senate Budget Committee (Feb. 10, 2000).

¹⁰ Opposition of the Rural Telecommunications Group and the Organization for the Promotion and Advancement of Small Telecommunication Companies (RTG/OPASTCO) at 4.

¹¹ 47 C.F.R. § 24.709(b).

¹² RTG/OPASTCO’s comments in this respect are inconsistent. After claiming that Auction No. 35 was an “overwhelming success,” they complain about “shell” companies that have “been allowed to exploit the Commission’s DE provisions.” Opposition of the Rural Telecommunications Group and the Organization for the Promotion and Advancement of Small Telecommunication Companies at 5. The Commission has rejected a challenge to the validity of one auction license awarded under these circumstances on the merits.

Together, these carriers constituted the top eleven bidders by net value, with high bids on 360 of the 422 available licenses in the auction.¹³ Because its members operate in small geographic areas, and cannot obtain additional funding from these larger carriers, the Rural Cellular Association has concluded that there are “more effective tools available to the Commission than closed bidding,” including bidding credits.¹⁴

T-Mobile and Professor Wilkie correctly maintain that the set-aside rules create an additional set of perverse incentives, encouraging both speculative overbidding and a “hold out” problem, causing billions of dollars of harm to consumer welfare.¹⁵ While there is a fiction that many DEs can make it by themselves, the history of bankruptcies and the “flipping” of C Block licenses belie this claim. Recently, Northcoast Communications assigned 50 PCS licenses, including 45 licenses that it won in closed bidding, to Verizon Wireless for \$750 million in cash.¹⁶ In another transaction valued at \$4.7 billion when it was consummated, TeleCorp PCS transferred a number of C and F Block PCS licenses won in closed bidding to AT&T Wireless when they merged.¹⁷ In short, the set-aside rules create a layer of middlemen for no economic purpose, except perhaps to provide a windfall for middlemen.

See In the Matter of Application of DCC PCS, Inc., File No. 0000365171, Auction No. 35 – C & F Block Broadband PCS, Order (Rel. June 12, 2003). Notably, TPS Utilicom, Inc., a DE who brought the challenge, subsequently defaulted on its four winning bids in Auction No. 35.

¹³ Data derived from *Top 15 Bidders by High Net Bids*, available at <http://wireless.fcc.gov/auctions/35/>. The national or regional carriers included Verizon Wireless, VoiceStream, and Leap Wireless International. The DEs (and the carriers that backed them) were Alaska Native Wireless (AT&T Wireless), Salmon PCS (Cingular), DCC PCS (Dobson Communications Corporation), Cook Inlet (VoiceStream), Black Crow Wireless (U.S. Cellular), SVC BidCo (Sprint), Lafayette Communications (Triton PCS), and Northcoast Communications (Cablevision). *See John Rockhold, Auction Masquerade – Government Activity*, Wireless Review (Feb. 1, 2001). In his Declaration supporting T-Mobile’s comments, Simon Wilkie notes that a firm must take on debt in order to meet the Commission’s eligibility requirements, and in a “best case scenario” a highly leveraged, under-capitalized firm will become the 7th competitor in the wireless market. Declaration of Simon J. Wilkie at ¶ 18 (Jul. 30, 2004). Leap Wireless International, as “one of the original Entrepreneur Block PCS providers,” represents the closest approximation to this “best case scenario.” Public Notice, WT Docket No. 03-263. Of course, Leap is just now reemerging from bankruptcy protection.

¹⁴ Comments of the Rural Cellular Association at 3.

¹⁵ Comments of T-Mobile USA, Inc., Executive Summary; Declaration of Simon J. Wilkie at ¶¶ 3-4.

¹⁶ *In re Applications of Northcoast Communications, LLC and Cellco Partnership d/b/a Verizon Wireless For Consent to Assignment of Licenses*, WT Docket No. 03-19 (Rel. Apr. 8, 2003). 3 of the licenses were obtained in Auction No. 35, discussed *supra*. The other 42 licenses were obtained in Auction No. 11 and subject to the entrepreneur eligibility rules, but not subject to transfer restrictions because Northcoast had satisfied the Commission’s five-year construction requirement. *Id.* at ¶ 7.

¹⁷ *See* Eighth Competition Report, *supra* n. 7, at ¶ 42.

Conclusion

Open bidding allows spectrum to be allocated to those who value it the most, while allowing auction participants to efficiently aggregate private information.¹⁸ To the extent that the Commission is required by statute to give favorable treatment to certain entities, bidding credits would appear to be preferable. Indeed, Professor Wilkie concludes that the application of standard antitrust principles or bidding credits “are much more effective mechanisms to achieve Congress’ goals of efficient use of the spectrum and diversification in the spectrum ownership.”¹⁹ These mechanisms, acting in concert with the Commission’s efforts to create secondary markets through the leasing of spectrum rights and expedited approval procedures,²⁰ should minimize information and error costs while meeting the Congressional goal of allowing small businesses to fully participate in the auction process.²¹ The Commission should therefore grant the petition and allow, once and for all, an open, free market in spectrum to flourish.

Respectfully submitted,

Adam M. Peters
Research Fellow & Regulatory Counsel
The Progress & Freedom Foundation
1401 H Street, NW
Suite 1075
Washington, DC 20005
(202) 289-8928
(202) 289-6079 Facsimile

August 8, 2004

¹⁸ See Declaration of Simon J. Wilkie at ¶ 3.

¹⁹ *Id.* at ¶ 5.

²⁰ *In the Matter of Promoting Efficient Use of Spectrum Through Elimination of Barriers to the Development of Secondary Markets*, Report and Order, WT Docket No. 00-230 (Rel. Oct. 6, 2003); News Release, *In the Matter Promoting Efficient Use of Spectrum Through Elimination of Barriers to the Development of Secondary Markets*, Second Report & Order, Order on Reconsideration, and Second Further Notice of Proposed Rulemaking, WT Docket No. 00-230 (Adopted Jul. 8, 2004). In his statement supporting the *Second Report and Order*, Chairman Powell noted that “our new rules will allow potential entrants greater opportunities to obtain much needed spectrum and create an environment where they can tailor their services according to customer’s needs.”

²¹ See Sixth Report and Order, *supra* n. 3, at ¶ 22:

Finally, Section 309(j)(4)(D) does not require the Commission to ensure that licenses actually are granted to small businesses but, rather, requires only that these small businesses be given the opportunity to participate in the provision of spectrum-based services.